

March 22, 2007

To: House Taxation Committee

From: Shirley J. Warehime, CPA
Montana Society of Certified Public Accountants

Re: SB 514

The Montana Society of Certified Public Accountants supports SB 514.

Form 1099G

New Section 1 regarding Federal Form 1099G is important to provide married taxpayers, who file separately on the same form, with refund information that is consistent with what actually happened and reflects the net refund, if any, reported on the tax return.

Married taxpayers file separately on the same tax form when each spouse has taxable income because Montana does not have a joint rate table. The form is designed so that the income tax due by each spouse is combined. The income tax paid by each spouse from withholding or estimate payments is also combined and offset against the combined tax due. The result is either the net combined tax due or overpaid. The overpayment is refunded or applied to the next year's estimated tax as directed by the taxpayers. Married taxpayers do have the option of filing on separate forms if they do not want the combining of their tax liability and taxes paid.

The current practice of the Montana Department of Revenue is to prepare Federal Form 1099G on a basis that ignores the combining of tax liability and payments when married taxpayers file separately on the same form. This creates a situation that is confusing to the taxpayers and does not reflect their perception of the filed tax return. It further complicates the reporting of refund information on the federal return and may lead taxpayers to over report income. Those who prepare tax returns frequently are asked—What is this form? We did not receive a REFUND” or “A refund of this AMOUNT”.

Attached is a letter by Walter J. Kero, Chair State Taxation Committee of the Montana Society of Certified Public Accountants to the Senate Taxation Committee that explains this situation in greater detail.

Penalty and Interest Computation

We concur with the changes in this section. Accruing interest and penalty on a “daily basis” is easier to compute and more equitable to the taxpayer than the current “month or fraction thereof” method.

Taxability of Federal Refunds on Montana Return

Section 3—(7) ~~old~~—this section is no longer applicable so should be removed.

Section 3—(7) **new**—These provision are needed so that all taxpayers are treated in a similar manner as to the taxability of Federal refunds on Montana returns. While the Montana Department of Revenue has agreed and is placing these provisions in the Department rules and regulations, we are more comfortable with them in statute.

Estimate Tax Payments

We concur with the reduction of penalty when the taxpayer makes approximately equal quarterly installments of estimated tax equal to 90% of the current year's tax or 100% of the prior year tax. This will give taxpayers assurance that if they comply with the estimate payment rules, they will not be penalized for underpayment of estimated tax.

February 21, 2007

Senator Elliott, Chair
Senate Taxation Committee
Helena, Montana

Re: Senate Bill 514

Dear Senator Elliott,

We write the following in support of Senate Bill 514 for the following reasons.

Simplification and Prevention of Overpaying Federal Tax

First, new section 1 (2) regarding forms 1099G will simplify Montana taxpayers filing their Federal tax returns and minimize the potential for Montana taxpayers from accidentally overpaying Federal taxes. The 1099G forms for 2006 issued by the Montana Department of Revenue reports refunds on a gross basis even though the State of Montana never issues a check to the taxpayers' for the amount shown on the 1099G.

The confusion happens when one taxpayer on a married filing separate return (both taxpayers are filing on the same form) has a balance due and the other taxpayer has a refund. The current 1099G forms are reporting the refund at gross but the check for the refund to the taxpayers' is written at the net amount. For example, if a taxpayer has a Montana refund from 2005 of \$1,500 and the spouse has a tax due of \$800, then the Department of Revenue issued a 1099G form in the amount of \$1,500. Taxpayers may overstate their Montana refund on their 2006 Federal return if they do not take into account the \$ 800.00 of Montana tax withheld from the \$1,500 overpayment. The potential overpayment of Federal tax is assuming a 25% Federal tax bracket would be \$200 in the above case ($\$ 800.00 \times 25\%$).

We quote Black's Law Dictionary for the definition of offsets. "Offset. A deduction; a counterclaim; a contrary claim or demand by which a given claim may be lessened or canceled. A claim that serves to counterbalance or to compensate for another claim. The law dictionary definition makes for some common sense on the 1099G issue. The Department of Revenue has issued 1099G forms for Montana refunds issued to Montana taxpayers in 2006. The issued 1099G forms do not match the refund check sent to the taxpayers' nor does the 1099G form take into account the offset that the State of Montana Department of Revenue used to lessen the amount of tax due from either the taxpayer or the spouse. The 1099G forms for 2006 as issued by the Department of Revenue are going to cause tax preparers extra work steps to correctly report the taxable income from Montana refunds. We only hope that taxpayers who prepare their own tax returns do not overpay their Federal taxes as a result of these 1099G forms.

The Montana Department of Revenue used to prepare the 1099G form taking into account the right of offset and the 1099G would match the check that was issued to the taxpayers. It is unfortunate that computer software is the causation of all of this extra work, not only for tax preparers but also for legislators and the Department of Revenue. It is too bad that all of this was not avoided.

Simplification of Penalties

We appreciate the simplification of penalty calculations by the elimination of the fraction of a month and going to a daily accrual. This change is more in line with how the Federal tax laws are on penalties and interest calculations. We wish the State of Montana would just follow the Federal rules copycat the late filing and late payment statutes from Internal Revenue Code. However, SB 514 is a step in the right direction.

The draft of SB 514 that we have has the "or fraction of a month" lined out in Section 2 "15-1-216" (2) (a) relating to late pay penalties but is not lined out in (2) (b) regarding late penalties on taxes under chapter 30, part 2 chapter 53.

Simplification of Calculating Federal Refunds on Montana Tax Returns

The bill specifies the order of priority in calculating a tax benefit, if any, attributable to a Federal refund on a Montana tax return. The bill will generally follow the Federal computations regarding a State income tax refund under the Federal tax benefit rule. The Federal computation on State income tax refunds can get complex due to the alternative minimum tax. We do not have that complexity in Montana.

Other items

We agree with the bill cleaning up Montana law for now expired issues such as the Roth transition rules on conversion of traditional IRA accounts to Roth IRA accounts at 15-30-111 (7) before the effects of this bill.

We also support the change at 15-30-241 (5) (f) that interest on the underpayment of estimated tax is waived if the taxpayer pays 90% of the current year's tax or 100% of the prior year's tax either through withholding tax and/or estimated taxes. This change is in keeping with Federal tax law rules on calculation of penalties on underpayment of estimated taxes and we welcome the similarity.

We thank you for allowing us to provide this information to the Senate Taxation Committee.

Sincerely,

Walter J. Kero, CPA
Chair State Taxation Committee
Montana Society of Certified Public Accountants